



Bank of Canada (TSX:RY) and CIBC (TSX:CM) Release Quarterly Earnings This Week: What to Watch Besides Stable Earnings?

Description

The big Canadian stocks are some of the most treasured stocks on the TSX. Earnings are steady and balance sheets often look squeaky clean; *Fool* contributor [Joey Frenette](#) has a recent full rundown. External factors do weigh on the bank stocks: housing, personal debt, tariffs, currency fluctuation, and others.

Have you noticed that while the US dollar has soared, many of the Canadian bank stocks have limped along? Uncertainty is bad for markets in general and particularly for banks.

In refinancing my own mortgage, I did something I've never done before: I went with a variable rate that was 1.1% below prime. Bargain! I'm playing the spread game between the variable and fixed rates. If rates climb more but level off, there's a good chance that I will come out a winner by saving on interest payments.

To a certain extent, that's what the banks do when they borrow money only to lend it out to their customers, be they retail or wholesale (e.g., businesses).

The increased revenue from interest payments is offset by the increased risk in loan defaults. If that sounds ominous, it should. It's not good for anybody when loans don't get paid.

In a previous [article](#) I briefly mentioned Tier 1 capital ratio, which gauges whether riskier assets make up the bank's core (top tier) assets. A higher Tier 1 capital ratio makes fiscally responsible economists shudder.

In the aftermath of the 2008 financial crisis, **Royal Bank of Canada** ([TSX:RY](#))([NYSE:RY](#)) had Tier 1 capital ratio of 13%. The fact that this risk ratio dropped then crawled up as of late is part of a broader context on how much risk banks should take.

This Wednesday, when Royal Bank reports on its quarterly, will this risk metric dial up, down or stay the same? This is an important barometer from the largest big bank.

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017
Tier 1 capital ratio	13%	13%	13.3%	13.1%	11.7%	11.4%	12.2%	12.3%	12.3%

Source: Royal Bank Investor Relation Annual Reports

In the case of **Canadian Imperial Bank of Commerce** ([TSX:CM](#))([NYSE:CM](#)), the top dividend paying bank stock among the big five, the 2017 Tier 1 capital ratio was 12.1%, very close to Royal Bank. CIBC reports on Thursday.

Both quarterly reports will undoubtedly put earnings front and centre. Now you know of one other metric to monitor!

Earnings are boring for these two stocks

In the last 24 quarters, or six years, Royal Bank has tended to beat earnings forecasts by 2.6%. The worst actual earnings was when Royal Bank missed its forecast by 2.3%. That is remarkably consistent!

For CIBC, the downside risk for earnings is even more boring — I mean impressive. In the last 24 quarters, the biggest “miss” was a miniscule 1% below the forecast.

A compelling case for CIBC is that this bank tends to exceed earnings forecasts by as much as 13.8% in one recent quarter. Royal Bank did a less well with an earnings beat of 10%.

These two bank stocks are so stable that they actually buy each other's stocks as part of their wealth management businesses!

I am increasingly convinced that the average do-it-yourself investor should own some of the big five banks.

It is not a question of whether to buy either of these bank stocks, but when! As earnings estimates are so reliable, one simple “buy” rule is to wait until the forward price-to-earnings ratio drops below the trailing price-to-earnings ratio. Neither Royal Bank nor CIBC meet that criteria right now, so it's time to wait.

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